SENATE FISCAL AGENCY

SENATE FISCAL AGENCY
MEMORANDUM

DATE: March 12, 2008

TO: Members of the Michigan Senate

FROM: Deb Hollon, Fiscal Analyst

RE: Bond Issuances of the Michigan Department of Transportation

As a part of her budget recommendations for FY 2008-09, Governor Granholm proposed the issuance of $150.0 million in transportation bonds as an economic stimulus package. The Governor's justification for the new issuance is that revenue from the bonds would advance road and bridge projects forward in time and provide additional jobs over the next few years. This memo is designed to provide an overview of bonding and indebtedness for the Michigan Department of Transportation (MDOT).

Authority of the Michigan Transportation Commission

Act 51 of 1951 authorizes the Transportation Commission to issue notes or bonds for transportation purposes without the approval of the Legislature. These notes and bonds are not general obligation bonds, but are paid through specific funding streams such as the State Transportation Fund or Federal aid received by the state.

While legislative approval is not needed, Act 51 does require the Department to provide the Senate and House Appropriations Committees with a list of projects at least 30 days prior to the actual issuance of the bonds. In addition, after the bonds are issued, the Appropriations Committees must be notified of any change to the initial list of projects prior to Transportation Commission action on that change.

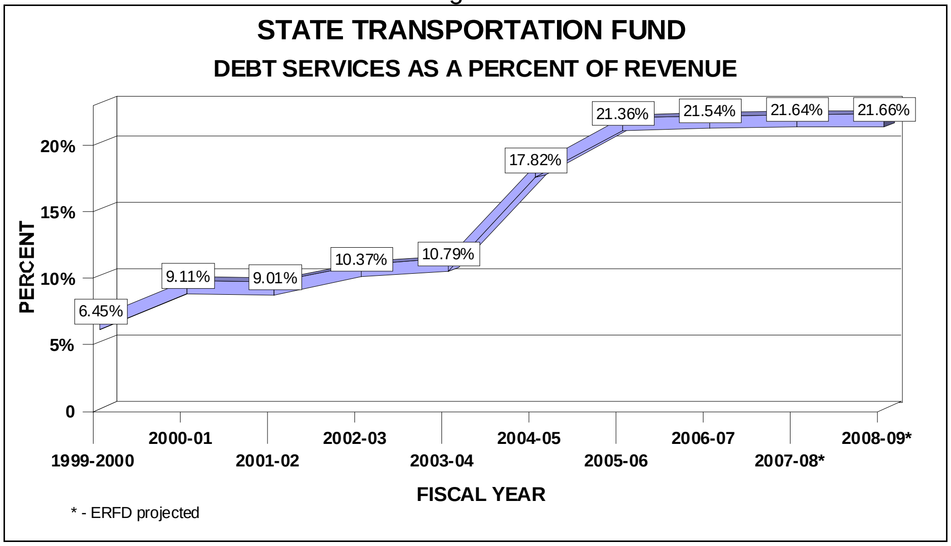
The Transportation Commission is tentatively scheduled to approve the economic stimulus bond issuance at its March meeting. The actual date of bond issuance will depend upon the fluctuations of the bond market and cash flow projections. The determination as to whether the bonds will be paid with State Transportation Fund (STF) revenues or Federal aid revenues will be made at the time of issuance and will also be a function of the bond market at that time.

Increased Use of Bond Financing

MDOT's level of STF debt service as a percentage of STF revenue has increased dramatically over the past ten years as seen in Figure 1. This increased use of bond financing has been a function of several factors: deceased revenue, increased costs, and the overall state of the economy. Over 95.0% of the revenue credited to the Michigan Transportation Fund (MTF) comes from motor fuel taxes and vehicle registration fees. The current Michigan motor fuel tax rates are 19 cents per gallon for gasoline and 15 cents per gallon for diesel fuel. (Comparison information concerning the fuel tax rates of other states can be found on the Senate Fiscal Agency website.)

201 N. Washington Square • Suite 800 - The Victor Center • Lansing, Michigan
Telephone: (517) 373-2768 • TDD: (517) 373-0543 • Fax: (517) 373-1986

Figure 1



Source: MDOT

Unlike the sales tax, which is a percentage of the dollar amount sold, the motor fuel tax rate is a fixed amount per gallon. As a result, an increase in the price per-gallon of fuel does not increase revenue to the MTF. In fact, as the per gallon price rises, consumer usage often decreases, which results in a decrease in State revenue from this source. One example of this effect can be seen after the surge in fuel prices following Hurricanes Katrina and Rita in 2005. Gasoline and diesel motor fuel tax revenue to the MTF dropped by over $20.0 million from fiscal year (FY) 2004-05 to FY 2005-06. Since that time, revenue from fuel taxes has continued to decline. Revenue from vehicle registrations has increased over the same time frame resulting in relatively flat overall revenue over the last few years. Table 1 reflects revenue to the MTF over the past ten years.

Table 1

Michigan Transportation Fund Revenue

Fiscal Year	Gasoline Tax Revenue	Vehicle Registration Revenue	Other Fuel Tax Revenue	Other Revenue	Total
1998-99	$931,031,120	$758,527,135	$135,364,353	$19,906,672	$1,844,829,280
1999-2000	921,991,065	802,945,158	144,521,335	23,112,879	1,892,570,437
2000-01	933,494,040	824,746,037	134,165,367	21,134,771	1,913,540,215
2001-02	938,911,784	877,074,423	143,868,807	14,379,470	1,974,234,484
2002-03	935,671,741	892,659,425	157,513,685	14,561,361	2,000,406,212
2003-04	932,139,677	978,527,057	141,139,542	12,776,784	2,064,583,060
2004-05	922,368,211	895,996,513	146,799,386	11,634,283	1,976,798,393
2005-06	906,220,722	898,798,415	149,171,067	13,729,483	1,967,919,687
2006-07	883,687,513	907,808,952	144,174,316	7,764,849	1,943,435,630
2007-08 Est.	867,000,000	911,550,000	146,950,000	6,100,000	1,931,600,000

While revenue for the MTF has remained relatively flat, the costs of construction have increased dramatically over the same time frame. According to the U.S. Department of Labor, Bureau of Labor

Statistics' Producer Price Index, overall prices for highway and street construction have increased by 58.1% from 1998 through 2007. Three major contributors to this increase are the prices for iron and steel, cement, and asphalt paving mixtures.

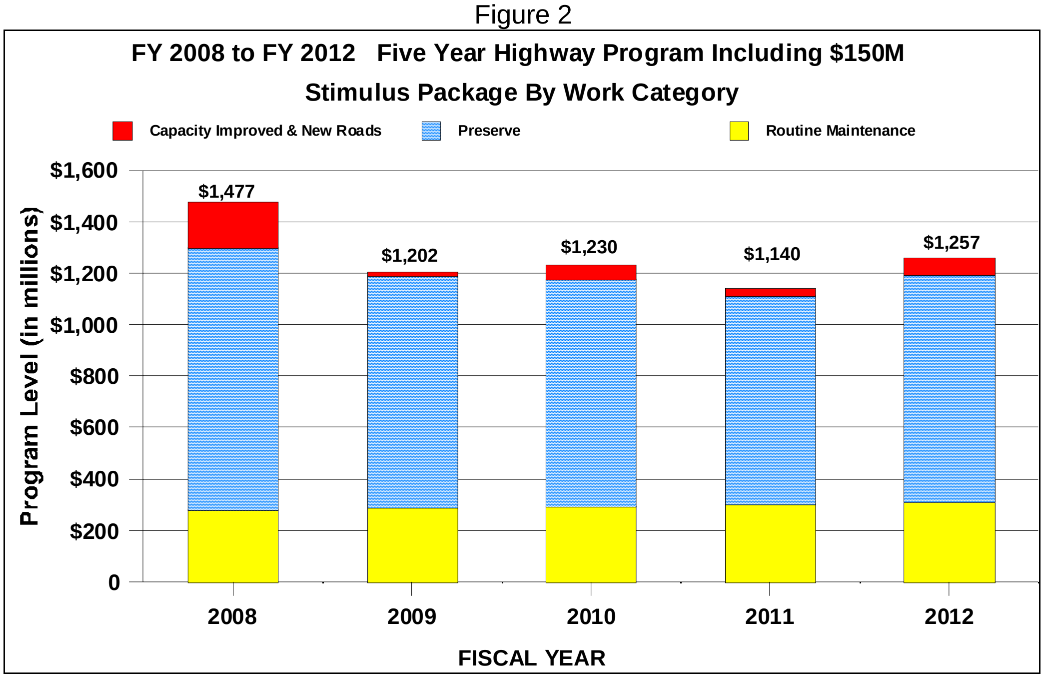
In addition to the rise in the prices of construction components, expenditures also have increased as projects have been accelerated in an effort to stimulate the economy by creating more construction jobs. The Jobs Today program, which was implemented in 2005, accelerated the timing of over 150 projects over two years. In addition, legislation enacted in 2006 created the Local Jobs Today program to provide increased loans and grants to local units of government to enable them to obtain Federal funding for transportation projects. The economic stimulus package proposed by the Governor as a part of her FY 2008-09 budget recommendation is also aimed at creating jobs in the construction industry.

An increase in the level of indebtedness is not a phenomenon limited only to Michigan. According to data on state obligations for highways compiled by the US Department of Transportation, Federal Highway Administration, Office of Highway Policy Information[1], Michigan's obligations more than doubled from 2002 to 2006. The national average increased by 42.8% over the same period. Of the surrounding states, Illinois also doubled its obligations while Minnesota saw a four-fold increase (It should be noted, however, that Minnesota's debt level is approximately one-fourth of Michigan's even with the increase.). Ohio's level of obligations remained level and Wisconsin's increased by approximately the same amount as the national average.

Implications for the Future

MDOT's stated pavement condition goal is to have 90% of State Trunkline roads and bridges in "Good" condition. This goal was surpassed in 2007 when 92% of the Trunkline was rated as "Good." However, as revenues continue to fall and construction costs continue to escalate, the Department will not be able to maintain this level of repair. According to the Department, an additional $460.0 million per year will be needed for road and bridge repair beginning in FY 2008-09 to maintain the Trunkline condition at 90% "Good." Figure 2 reflects the Five-Year Plan for the Highway Program, which was adopted by the Transportation Commission on February 28.

Figure 2



Source: MDOT

---

[1] Data used to facilitate state-to-state comparison might not match other figures in this document.

The debt service associated with the new $150.0 million bond issuance is estimated to be $14.2 million annually for 15 years. With that issuance included, debt service levels for road and bridge projects will be 23.2% of State Transportation Fund (STF) revenue (excluding Federal funds and projects). As more revenue is used for debt service, less is available for road and bridge repair and construction. STF debt service payments are expected to peak in FY 2009-10, but there won't be a significant decrease in those obligations until FY 2019-20. Unless new sources of revenue are found, either the condition of the Trunkline will begin to deteriorate or more bond revenue will be needed resulting in more debt service obligations and even fewer available funds for road and bridge work.

Attached is a listing of the current outstanding road and bridge bonds for the Department of Transportation (excluding Federal).

Please call should you have questions or need further information.

/wm

c: Gary S. Olson, Director
Ellen Jeffries, Deputy Director
Kathryn Summers-Coty, Chief Analyst

Outstanding Bonds Related to Road and Bridge Funding

The information below reflects outstanding bonds which were issued to fund road and bridge construction. This list includes bonds on which debt service is funded through the State Transportation Fund (STF) as well as bonds which were secured using STF revenue. Not included are transit or airport-related bonds secured or paid through the Comprehensive Transportation Fund or those bond issuances utilizing Federal revenues.

Year/Purpose	Fund Source	Average Annual Debt Service	Expected Payoff
1989 $135.8 million - State and local economic development projects; trunkline right-of-way projects	Transportation Economic Development Fund State Trunkline Fund	$4,580,586 $1,374,414	FY 2008-09
1992 $253.6 million - Build Michigan I	Critical Bridge Fund Transportation Economic Development Fund State Trunkline Fund	$1,416,525 $973,600 $10,319,875	FY 2013
1998 $377.9 million - Refinancing of previous bond issuances	Blue Water Bridge Fund Critical Bridge Fund Transportation Economic Development Fund State Trunkline Fund	$2,056,408 $1,327,737 $4,026,412 $21,390,674	FY 2026-27
2001 $308.2 million - Build Michigan III	Transportation Economic Development Fund State Trunkline Fund	$1,676,542 $5,774,755	FY 2011-2012
2004 $103.5 million - Refinancing of previous bond issuances	Blue Water Bridge Fund Transportation Economic Development Fund State Trunkline Fund	$79,229 $2,180,830 $7,897,509	FY 2021-22
2004 $185.7 million - Preserve First projects (first issue)	State Trunkline Fund	$10,174,905	FY 2018-19
2005 $378.3 million - Issuance of STF bonds to refund Federal anticipation notes issued for Build Michigan II	State Trunkline Fund	$43,245,424	FY 2018-19
2006 $244.5 million - Preserve First projects (second issue)	State Trunkline Fund	$23,157,375	FY 2021-22